S T A T E O F M I C H I G A N

STATE OFFICE OF ADMINISTRATIVE HEARINGS AND RULES

FOR THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of	)	
Consumers Energy Company for	)	Case No. U-16045
approval of a Power Supply Cost	)	
Recovery Plan and for authorization	)	
of monthly Power Supply Cost	)	
Recovery Factors for the year 2010.	)	

NOTICE OF PROPOSAL FOR DECISION

The attached Proposal for Decision is being issued and served on all parties of record in the above matter on July 16, 2010.

Exceptions, if any, must be filed with the Michigan Public Service Commission, P.O. Box 30221, 6545 Mercantile Way, Lansing, Michigan 48909, and served on all other parties of record on or before August 6, 2010, or within such further period as may be authorized for filing exceptions. If exceptions are filed, replies thereto may be filed on or before August 20, 2010. **The Commission has selected this case for participation in its Paperless Electronic Filings Program. No paper documents will be required to be filed in this case.**

At the expiration of the period for filing of exceptions, an Order of the Commission will be issued in conformity with the attached Proposal for Decision and will become effective unless exceptions are filed seasonably or unless the Proposal for

Decision is reviewed by action of the Commission. To be seasonably filed, exceptions must reach the Commission on or before the date they are due.

STATE OFFICE OF ADMINISTRATIVE
HEARINGS AND RULES
For the Michigan Public Service Commission

Sharon L. Feldman

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Sharon L. Feldman
Administrative Law Judge

July 16, 2010
Lansing, Michigan
dmp

STATE OF MICHIGAN

STATE OFFICE OF ADMINISTRATIVE HEARINGS AND RULES

FOR THE MICHIGAN PUBLIC SERVICE COMMISSION

* * * * *

In the matter of the application of **Consumers Energy Company** for approval of a Power Supply Cost Recovery Plan and for authorization of monthly Power Supply Cost Recovery Factors for the year 2010.	)	Case No. U-16045

PROPOSAL FOR DECISION

I.

PROCEDURAL HISTORY

This Proposal for Decision (PFD) addresses Consumers Energy Company's (Consumers) September 30, 2009 filing seeking approval of its Power Supply Cost Recovery Plan and factors for calendar year 2010.

The company's plan forecasts 2010 total system power supply costs of $1,717,229,489, and total system requirements of 35,634,977,000 kWh. In the plan as originally filed, the company also included approximately $25 million attributed to Rate E-1 underrecovery, and calculated a maximum PSCR factor of $0.02257 per kWh. The company subsequently revised its PSCR calculation, and is now seeking a maximum PSCR factor of negative $0.00052 per kWh,[1] reflecting the new base PSCR factor of $0.04866 per kWh set in Case No. U-15645, and the company's decision to drop its

[1] Also presented as ($0.00052) per kWh.

proposed Rate E-1 recovery. The company also seeks approval of two contracts, Exhibits A-19 and A-20. Consumers' filing included testimony and exhibits from eight witnesses, all company employees: Laura M. Collins, Andrew C. Dotterweich, Brian D. Gallaway, David B. Kehoe, Hubert W. Miller, III, Richard J. Polena, David F. Ronk, Jr., and Lincoln D. Warriner.

At the December 1, 2009 prehearing conference, the company and Staff appeared; the Michigan Environmental Council (MEC), the Attorney General, the Association of Businesses Advocating Tariff Equity (ABATE), Hemlock Semiconductor Corporation, Midland Cogeneration Limited Partnership, Michigan Power LP, Ada Cogeneration LP, and Cadillac Renewable Energy, LLC appeared and were granted intervention; and a schedule was established.[2] Following the established schedule, on March 11, 2010, MEC filed testimony from its consultant, George E. Sansoucy. Consumers filed rebuttal testimony from Ms. Collins, and Messrs. Gallaway, Polena and Ronk on April 2, 2010. Consumers also filed a revised Exhibit A-1 on March 24, 2010. Subsequently, on April 9, 2010, MEC filed surrebuttal testimony and exhibits from Mr. Sansoucy, accompanied by a motion; and on April 16, 2010, Consumers filed a response to the MEC motion accompanied by "second rebuttal" testimony from Mr. Gallaway.

At the hearing on April 20, 2010, Messrs. Gallaway, Ronk, Polena and Warriner appeared and were cross-examined, while the testimony of the remaining witnesses was bound into the record by agreement of the parties, without the need for the witnesses to appear. By agreement of the parties, both Mr. Sansoucy's surrebuttal

[2]A date for a motion regarding MCL 460.6a(7)-(9) was originally scheduled, and was adjourned at the request of the Attorney General by letter dated December 21, 2009.

testimony and Mr. Gallaway's second rebuttal, with accompanying exhibits, were included in the record. Consumers did not offer Mr. Miller's prefiled testimony and exhibits, which dealt with the Rate E-1 discount.[3]

Again following the established schedule, Consumers, MEC and the Attorney General filed briefs on May 13, 2010; Consumers, MEC, the Attorney General and Staff filed reply briefs on June 4, 2010.

The evidentiary record includes 298 transcript pages, and 54 exhibits. By agreement of the parties, official notice was also taken of the testimony of one witness (Michael Hoffman) from Case No. U-16047. A brief overview of the record is presented in section II below, followed by a review of the parties' positions in section III, and a discussion of each of the issues in section IV.

II.

<u>OVERVIEW OF THE RECORD</u>

The company's direct case included testimony and exhibits presented by seven witnesses. Ms. Collins presented the company's PSCR factor calculation, which is contained in Exhibit A-1.[4] Ms. Collins's exhibit divides total system power supply costs by total system requirements, subtracts the base recovery factor of $0.04866 per kWh set in Case No. U-15645, and then adjusts the result using a line loss factor of 1.086. Ms. Collins relied on Mr. Polena for the total system power supply cost forecast, on Mr. Dotterweich for the transmission expense forecast and the offsetting Schedule 2

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[3] See Tr 19.
[4] Ms. Collins is a Senior Rate Analyst for Consumers Energy. Her testimony is transcribed at Tr 23-30.

Reactive Revenues, and on Mr. Kehoe for the environmental expense forecast. She relied on Mr. Warriner for the total system requirements forecast.

Presenting the company's system power supply cost forecast, Mr. Polena testified that the company forecasts fuel and purchased and net interchange power needs using the "PROMOD" economic dispatch model.[5] Inputs to the model include data on system loads and generation requirements provided by Mr. Warriner, information on generation unit availability from Mr. Kehoe, and coal, oil and natural gas cost forecasts provided by Mr. Gallaway. Expected power purchases are estimated using delivery history for non-dispatchable supplies, and using modeling similar to the modeling of company-owned generation for dispatchable supplies. Exhibit A-14 contains the 2010 forecast on a monthly basis; Exhibit A-15 contains the annual forecast for the five-year period 2010-2014. Exhibit A-16 shows the company's purchase power agreements in place for 2010, with summary information on the capacity, energy and administrative charges associated with each contract.

Mr. Gallaway presented the company's projected fuel costs, including the expected cost of coal, oil and natural gas for the five-year forecast period, with a discussion of actions the company takes to minimize these costs.[6] Exhibit A-3 summarizes the company's coal contracts, with 2010 as-burned coal cost projections presented in Exhibit A-4 and 2011-2014 cost projections in Exhibit A-6. Oil and gas cost projections for 2010 are presented in Exhibit A-5, with 2011-2014 cost projections presented in Exhibit A-7.

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[5] Mr. Polena is Principal Engineer Lead in the Electric and Gas Supply Department; his testimony is transcribed at Tr 204-236.

[6] Mr. Gallaway is the Fuels, Transportation and Planning Director in the Electric and Gas Supply Department; his testimony is transcribed at Tr 42-150.

Mr. Kehoe testified regarding the company's planned outages and forecast outage rates, as well as the environmental expenses associated with the company's air emission's allowances, including NOx allowances and urea expenses.[7] The planned major outages are shown in Exhibit A-9, while the forecast random outage rate underlying the 2010 cost projections is shown in Exhibit A-8. As noted above, the outage rates were used by Mr. Polena to model planned sources of supply. Exhibit A-10 shows the company's forecast of the NOx allowance expenses and Exhibit A-11 the forecast of the urea expenses. The 2010 forecast environmental expenses are included on line 7 of Exhibit A-1.

Mr. Ronk presented an overview of the company's planned sources of electric generation, and discussed the company's seasonal planning reserve margin target.[8] Based on MISO determinations, the company intends to maintain a 12.69% reserve margin. Mr. Ronk's Exhibit A-17 shows the resources by category expected to be available to meet the summer peak capacity, including expected loads and reserve margins, for 2010 through 2014. As shown in this exhibit, the company projects a 2010 summer peak capacity reserve margin of 18.6%. Mr. Ronk testified that the company does not need additional capacity for the summer of 2010, but has sold some, and expects to sell additional capacity to reduce its summer peak reserve margin to 12.69%.

Mr. Ronk testified as to how the PSCR plan treated costs associated with the company's "Green Generation" program, approved in Case No. U-13843, and its renewable energy plan, approved in Case No. U-15805. He further testified in support of

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[7] Mr. Kehoe is Director of Staff, in Electric Generation for Consumers Energy. His testimony is transcribed at Tr 261-273.
[8] Mr. Ronk is Director of Electric Transactions and Resource Planning; his testimony is transcribed at Tr 151-203.

two agreements the company seeks approval for, Exhibit A-19, a long-term power purchase agreement with the Scenic View Dairy—Fennville, and Exhibit A-20, a reduced dispatch agreement with Ada Cogeneration. Mr. Ronk also explained that the company's plan includes renewable resource agreements that were pending approval in Case No. U-15805. It appears these agreements were approved in that docket by Commission order dated October 13, 2009.

Mr. Ronk's testimony also addressed anticipated MISO charges and revenues, explaining that while the company has been able to project or estimate many elements of the MISO settlement charges, the company intends to include all such charges in the PSCR cost reconciliation. His Exhibit A-18 illustrates MISO settlement charges on a typical statement.

Mr. Dotterweich was the company's main witness on expected MISO charges.[9] He testified regarding the transmission costs included in the PSCR factor calculation. He detailed projected MISO charges of $248,234,653 for 2010 in Exhibit A-2, also reflected in line 2 of Exhibit A-1. Mr. Dotterweich also explained the company's offsetting credit of $19,706,000 attributable to "Schedule 2 Reactive Revenues" associated with the ROA program, which is shown on line 3 of Exhibit A-1.

Mr. Warriner presented Consumers' official forecasts of electric deliveries, generation requirements, and peak demand for the 2010 to 2014 period.[10] He testified these forecasts were approved by management in July, 2009, and are based on a combination of regression analysis, customer input, and professional judgment, with

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[9] Mr. Dotterweich is the Director of Electric Transmission and Market Regulations in the Electric and Gas Supply Department; his testimony is transcribed at Tr 32-41.

[10] Mr. Warriner is Senior Business Support Consultant-Lead in the Rates and Business Support Department; his testimony is transcribed at Tr 236-259.

explicit consideration of energy efficiency and the potential for plug-in hybrids. Exhibit A-21 presents the monthly calendar-year deliveries forecast for 2010, including ROA and full service projections, while the annual forecasts for 2010-2014 are presented in Exhibit A-22. Peak demand forecasts are presented in Exhibit A-23, and monthly generation requirements are presented in Exhibit A-24 for the period 2010-2014. Exhibit A-25 presents other miscellaneous forecasts.

MEC's witness, Mr. Sansoucy, was the only witness to challenge the company's plan.[11] Mr. Sansoucy raised four objections to the company's plan in his direct testimony. First, he testified that Consumers' projected line loss for 2010 of 8.6% is excessive in comparison to a 13-utility sample of other regulated utilities, is higher than Consumers reported in a 2008 FERC filing, and has not improved over time. He presented Exhibits MEC-1 through MEC-5 and MEC-13 in support of this testimony. Mr. Sansoucy recommended using the 13-utility average line loss factor to compute the PSCR factor, resulting in a $27 million reduction in PSCR costs as shown in his Exhibit MEC-6.

Second, Mr. Sansoucy testified that Consumers' coal cost projections for 2010 are excessive, 28% higher than Detroit Edison's projected coal cost for 2010, and higher than national forecasts. His Exhibit MEC-7 contains Consumers' coal purchase specifications; Exhibit MEC-8 contains a national coal price forecast for 2010; and Exhibit MEC-9 is Detroit Edison's 2010 plan case coal forecast as presented in Case No. U-16047. Mr. Sansoucy recommended that the Commission reduce Consumers'

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[11] Mr. Sansoucy is a registered professional engineer and head of his own consulting firm. His testimony is transcribed at Tr 276-295.

forecast to the level of Detroit Edison's forecast; MEC-10 presents his resulting recommended $107 million reduction in Consumers' PSCR costs.

Third, Mr. Sansoucy testified that Consumers' projected cost of natural gas for its Zeeland plant is excessive. His Exhibit MEC-11 presents the NYMEX strip Consumers identified in discovery as the basis for its cost projection. Mr. Sansoucy further testified that he expected prices to fall due to a "glut" in the natural gas market. His Exhibit MEC-12 presents his recommended reduction in PSCR costs of $5,108,659.

Fourth, Mr. Sansoucy testified the company has excessive company-owned generation that is not being efficiently utilized. He looked at FERC filings and Consumers' plan and discovery responses to conclude that the company is increasingly relying on purchased power, and that the company's utilization of its own generation assets is falling, despite declining utility sales. He concluded that the company's utilization of its power plant capacity is only 33%, while its utilization of the capacity available under contract is almost 100%. He relied on the data presented in Exhibits MEC-1, MEC-2, MEC-3, MEC-4 and MEC-13, along with data presented in the company's plan. He recommended that the Commission order an investigation of the company's dispatching to maximize the cost effectiveness of its plants, or in the alternative reduce PSCR costs by 8%, which he testified represents the difference between the sales the company estimated in its 2010 plan, and the sales it reported in discovery. He relied on additional data presented in Exhibit MEC-14 to support his claim that Consumers has reduced its sales forecast by 8% since the plan filing.

In rebuttal testimony, Ms. Collins and Mr. Ronk addressed the line loss factor issue raised by Mr. Sansoucy. Mr. Ronk testified that the company's line loss factor is not excessive. Ms. Collins testified that the line loss factor is mandated by the company's tariff, and also that through the reconciliation process, customers would be charged only for actual line losses.

Mr. Polena addressed Mr. Sansoucy's contention that the company's plan includes excessive costs attributable to company-owned generation. Mr. Polena testified that the company's utilization of contract capacity is approximately 47% rather than 100%. He further testified that the company's utilization of its coal-fired generation plants is approximately 78%, while its utilization of its oil and gas "peaking" units is 5%. Mr. Polena also testified that the company had not changed its 2010 sales forecast since it filed its plan, but that Mr. Sansoucy's conclusion was based on an improper comparison of "total system" or generation requirements in Exhibit A-1, with the full service sales projection provided in MEC-14. Mr. Polena's Exhibits A-27 and A-28 present additional FERC filing information to support Mr. Polena's recalculation of the percent of purchased capacity the company actually uses.

Mr. Gallaway's rebuttal testimony addressed the company's coal and natural gas purchasing and cost projections, to refute Mr. Sansoucy's claims that the company's projected costs are excessive and its practices imprudent, and contending that Mr. Sansoucy's analysis was erroneous. His Exhibit A-26 compared Detroit Edison's and Consumers' coal plants.

In surrebuttal testimony, admitted by agreement of the parties, Mr. Sansoucy presented additional evidence regarding natural gas and coal costs. His Exhibit MEC-15 is an excerpt from an ANR pipeline FERC tariff, while Exhibit MEC-16 contains a DOE report on gas prices into Michigan; Exhibits MEC-17 and MEC-18 are excerpts from Consumers' 2009 PSCR reconciliation, showing 2009 actual natural gas and coal costs.

Mr. Gallaway's second rebuttal testimony, also admitted by agreement of the parties, likewise addressed coal and natural gas costs. Mr. Gallaway provided further testimony regarding natural transportation and commodity costs for Consumers, and regarding Mr. Sansoucy's comparison of DTE coal costs to Consumers' projections. His Exhibit A-29 is an additional excerpt from an ANR FERC tariff; Exhibit A-30 shows natural gas prices over time, and in comparison to the company's PSCR plan projection.

Completing the record on these issues, Exhibits MEC-19 through MEC-26 were admitted at the hearing; by agreement of the parties, official notice was taken of the testimony of Detroit Edison witness Michael Hoffman in Case No. U-16047, Detroit Edison's 2010 PSCR plan case.

III.

POSITIONS OF THE PARTIES

In its briefs, MEC challenges the coal and natural gas cost projections included in Consumers' plan, and seeks reductions of $97 million in the utility's 2010 coal cost projection and $17.5 million in the utility's 2010 natural gas costs, which MEC attributes to imprudence by the company. In addition, MEC argues that the company's 2010 sales forecast is overstated, and was overstated when filed, and asks the Commission to find the sales forecast unreasonable.[12]

Consumers argues that its coal and natural gas purchases are reasonable and prudent, and disputes MEC's contentions that the projected costs are excessive. Consumers addresses MEC's challenges to the utility's coal and natural gas purchases in both its brief and reply brief; Consumers does not address MEC's contentions regarding the 2010 sales forecast, raised for the first time in MEC's initial brief, except to claim that MEC's argument is untimely.

Staff's reply brief supports the company's plan and forecast, and in particular addresses MEC's objections to the utility's coal and natural gas cost projections.

The Attorney General's briefs address MCL 460.6a, subsections (7), (8) and (9). He requests that the Commission take additional steps in this proceeding to preserve the parties' rights to review in the reconciliation proceeding the reasonableness and prudence of payments to biomass merchant plants under these provisions, recognizing the Commission has already addressed this in its August 11, 2009 order in Case No. U-16048. Staff argues that the Attorney General's request is unnecessary, while Consumers seeks a determination that its "projected amounts" for the additional expenses are reasonable, recognizing that the reasonableness and prudence of the expenses remains an issue for reconciliation.

Additionally, in his reply brief, the Attorney General supports MEC's coal and natural gas cost reductions. He joins MEC in requesting a determination that the

[12] At the April 20 hearing, MEC indicated that it would not pursue one of the issues raised in Mr. Sansoucy's direct testimony, the line loss issue. In its briefs, MEC also does not pursue Mr. Sansoucy's contention regarding the company's utilization of its generation assets.

company's sales forecast is unreasonable, and requests that the Commission require Consumers to "specifically explain future increases in sales."

The positions of the parties, and the record evidence on the disputed issues, are discussed in more detail below.

IV.

DISCUSSION

In the discussion that follows, coal costs are addressed in section A, followed by a discussion of natural gas costs in section B. Section C discusses the 2010 sales forecast. Section D discusses Consumers' forecast payments to the biomass merchant plants in light of the Commission's order in Case No. U-16048. Section E discusses the requested contract approval.

A. Coal Costs

As indicated above, MEC challenges Consumers' projected coal costs for the plan period, and seeks a $97 million reduction in PSCR costs. The lynchpin of MEC's claim is that Consumers' projected coal costs for 2010 are significantly higher than Detroit Edison's projected coal costs for the same period.

The parties agree that Consumers' plan projects as-burned coal costs of approximately $2.45 per million Btu in 2010.[13] Comparing this cost to the estimated $1.96 per million Btu coal cost projection in Detroit Edison's 2010 plan case, MEC

[13] Mr. Sansoucy originally calculated $2.52 per million Btu as the average coal cost in Consumers' plan, using contractual minimum coal quality specifications (Btu content) provided in Exhibit MEC-7; MEC's brief adopts Mr. Gallaway's $2.45 figure, computed using the company's expected average coal quality.

emphasizes that Consumers' projected costs are 25% higher than Detroit Edison's. Mr. Sansoucy testified:

> Where both companies operate in the same state, have access to similar port facilities, and operate similar coal fired power plants, this difference is not reasonable and is conclusive evidence that the company has not taken all appropriate actions to minimize the cost of fuel.[14]

In its brief, MEC argues: "There is nothing in this record that justifies such a large disparity or provides any compelling reason why the comparison is not a relevant factor in evaluating the reasonableness and prudence of Consumers' projected costs." MEC's proposed $97 million power supply cost reduction results from using Detroit Edison's lower $1.96 per million Btu cost estimate to price Consumers' 2010 plan case coal volumes. The Attorney General agrees with MEC's analysis.

Consumers contends in response that MEC's comparison of Consumers' coal costs to Detroit Edison's is "a tendentious comparison", and does not provide any meaningful information to the Commission in reviewing the decisions underlying the company's plan. Consumers challenges Mr. Sansoucy's conclusion that Detroit Edison's lower costs constitute "conclusive evidence" that Consumers has been imprudent, disputing his broad statement that the utility's are "similar". Mr. Gallaway testified in this regard that the companies are only similar "in the geographical sense", and provided examples to show why it is not reasonable to assume that Consumers and Detroit Edison would have the same cost of coal, including plant-specific air pollution permits, different coal delivery points with different transportation options, differing ages and sizes of plants, and other differences in the utility's cost structures. Consumers emphasizes that all its coal and coal transportation contracts have been competitively

[14] See Tr 283-4.

bid, and argues that MEC has not provided any connection between the company's decision-making process, the focus of Act 304, and the alleged excess costs of coal.[15] Staff supports the company's analysis, asserting that MEC's "surface level" comparisons fall short of evaluating the prudence of the utility's decisions.

This PFD recommends that the Commission reject MEC's requested coal cost adjustment. A difference, even a 25% difference, in coal costs between the state's two largest utilities is not sufficient to establish that Consumers' coal purchases have been unreasonable or imprudent. Under Act 304, plan proceedings provide an opportunity for the parties and the Commission to review the decisions underlying the company's plan and five-year forecast:

> In its final order in a power supply and cost review, the commission shall evaluate the reasonableness and prudence of the decisions underlying the power supply cost recovery plan . . . and shall approve, disapprove, or amend the power supply cost recovery plan accordingly.[16]

As Consumers and Staff argue, a broad-brush comparison to Detroit Edison does not identify or take issue with any decision or planned decision-making of the utility.

Note that in its plan filing, Consumers identified only 14 annual and longer-term coal purchase contracts and six coal transportation contracts, which along with spot market purchases cover the utility's principal coal cost components.[17] These 20 contracts, and the company's planned spot purchases, reflect key decisions reviewable in PSCR plan cases. Mr. Gallaway and Mr. Polena also explained that the company

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[15] See Consumers' reply brief at 5-6.
[16] See MCL 460.6j(6). Likewise, the Commission is to "evaluate the decisions underlying the 5-year forecast" under MCL 460.6j(7).
[17] Costs for auxiliary fuel, dust control and state air emissions fees are shown separately on Exhibit A-4.

uses sophisticated modeling that takes into account fuel needs, heat rates and plant efficiencies to determine its coal purchase requirements.

In contrast, MEC has not supported its contention that it is reasonable to expect the two utilities to have the same coal costs. For Consumers, coal costs constitute almost 30% of its proposed total system power supply costs.[18] As Mr. Gallaway explained, the two utilities do not have the same plants, the same fuel mix—which is driven by plant design and operating constraints, or the same transportation options. The two companies do not necessarily make the same choices about the mix of contract versus spot market purchases, or the timing of these purchases.

In their briefs, both MEC and the Attorney General argue instead that once the cost difference is identified, Consumers bears the burden to provide a detailed, quantitative analysis of the reasons for the difference. The Attorney General emphasizes that the burden of proof, including the burden of persuasion, remains with Consumers, and asserts that the company has not met this burden:

> CECo's costs are significantly higher than DECo's, and Mr. Gallaway does not quantify how and why the differences he describes result in higher costs. At best, CECo's arguments leave the Commission to speculate that the identified differences do in fact require CECo to pay more—they may do so—but CECo has not demonstrated by a preponderance of the evidence that the differences do require CECo to pay much more.[19]

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[18] $497,901,479 as-burned coal cost figure from Exhibit A-4 divided by total system power supply costs of $1,717,229,489 from Exhibit A-1.

[19] See Attorney General's reply brief at 5. See also MEC brief at 18: "If the company plans to charge its customers almost $97 million more for coal than Detroit Edison would, the company needs a better explanation than any it has offered in this case."

Consumers, however, has established on this record that its coal and coal transportation contracts were established by competitive bidding.[20] Neither MEC nor the Attorney General have presented any evidence that the competitive bidding process used by Consumers was deficient in any respect. Nor have MEC or the Attorney General presented any argument supported by evidence of record that the mix of contract and spot market purchases or the timing of these purchases has been or will be unreasonable or imprudent. Likewise, no party has challenged the modeling results leading to decisions about the types of coal the company purchases. The mere fact that Detroit Edison's coal and transportation costs are lower does not give rise to an inference that the coal and coal transportation decisions underlying Consumers' plan are unreasonable or imprudent.

As noted above, Act 304 requires a utility to justify the decisions underlying its plan—it must explain its decisions and provide evidence to show that the decisions are reasonable—but it is not required to provide a comparison with other utilities as a part of its plan. Were Consumers required to make the detailed showing called for by MEC, it must come at the rebuttal phase of the plan case proceeding. Given the numerous potential reasons for the difference, it is not reasonable to expect Consumers, within the time frame of rebuttal in a plan case, to provide a comprehensive analysis reconciling its coal requirements to those of Detroit Edison. It is not even clear that Consumers would have access to the information necessary to conduct such an analysis. Note that the Hoffman testimony officially noticed from Detroit Edison's plan case does not provide many of the details such an analysis would require. MEC, for example, faults Mr.

[20] See Tr 55, 67.

Gallaway for not knowing heating rates associated with DTE plants, when MEC obtained heat rate information for Consumers' plants in response to discovery.[21] MEC also faults Mr. Gallaway for not identifying the percentage of Detroit Edison's eastern coal purchases that come from lower-cost Northern Appalachian suppliers,[22] and for not having personal knowledge to support his belief that Detroit Edison's expected increase in coal costs in 2011 is due to new transportation contracts.[23]

Merely substituting Detroit Energy's costs in Consumers' factor calculation, as MEC and the Attorney General request, also gives no guidance as to how such costs would be reconciled. Were this adjustment to be adopted, would Consumers' PSCR reconciliation presume that the utility could achieve Detroit Edison's planned costs? Would it presume that the utility could achieve Detroit Edison's actual costs? Must Consumers' reconciliation await the completion of Detroit Energy's reconciliation? The difficulty correlating MEC's recommended cost reduction with the review to occur in the reconciliation shows the difficulties associated with an adjustment that is not based on identifiable utility decision-making as contemplated by MCL 460.6j(6).

Nonetheless, having reached the conclusion that Consumers is not required to provide a quantitative evaluation of the differences between its as-burned coal costs and Detroit Edison's in order to meet its burden of proof in this plan proceeding, this PFD finds it appropriate to review the evidence Consumers did present in greater detail, to address MEC's claim that "none of these reasons—individually or collectively—

[21] See MEC brief at 16-17.
[22] See MEC brief at 10.
[23] See MEC brief at 13.

account for the size of the difference" between the two utilities.[24] Coal purchasing strategies, coal types, and transportation cost differences are discussed in subsections 1, 2 and 3 below.

1. "Layering" of purchases

Consumers and Detroit Edison each have a mix of coal purchase contracts, with different beginning and ending dates. Mr. Gallaway referred to this as layering, and explained:

> The portfolio for a given year will consist of contracts of various vintages, with various volumes, term lengths, and prices. . . . In as much as these purchases were competitively bid, the pricing of these contracts is reflective of the market at the time the purchase was made. As with any portfolio, some components of the portfolio may be above market and some may be below market at any given time, depending on how the current market has changed relative to the time the original purchase was made.[25]

Consumers presented this testimony principally to rebut Mr. Sansoucy's testimony that Consumers' coal costs were unreasonable in part because they were above national coal price estimates.[26] MEC rejects layering as an explanation for cost differences between the utilities, since both utilities engage in the practice.[27] But the differences in time and length of coal contracts—or transportation contracts—cannot be readily dismissed on the basis that both companies have contracts of different vintages, and also purchase coal on the spot market. Notably, neither MEC nor the Attorney General presented any evidence that the layering decisions made by Consumers were unreasonable or imprudent.

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[24] See MEC brief at 6.
[25] See Tr 67.
[26] Mr. Sansoucy provided Exhibit MEC-8 to support his testimony; MEC's brief does not claim that Consumers' costs are unreasonable simply because they are above current market prices.
[27] See MEC brief at 7 n5, citing Hoffman, page MGH-6, Case No. U-16047.

Consumers provided testimony on its coal purchasing strategy:

> Consumers Energy purchases and secures quantities over time that typically enable it to have ~70% to 90% of its anticipated volume secured by the fall of each year for the following calendar year; ~40% to 50% secured for the next calendar year, and ~20% to 25% secured for the next calendar year.[28]

Consumers also purchases approximately 88% of its total coal requirements from its contract or annual suppliers, with 12% percent purchased on the spot market.[29] There is no comparable testimony from Mr. Hoffman on behalf of Detroit Edison in the officially-noticed portion of the record in Case No. U-16047, but there is no reason to believe Detroit Edison makes its purchases using the same structure.

Note that the contract data shown in Exhibit A-3 for Consumers and listed in Mr. Hoffman's testimony for Detroit Edison do not establish when the contracts were negotiated. And contract prices can vary significantly. The "FOB mine" prices listed in Mr. Hoffman's testimony for Detroit Edison's contracts show a range of 55 cents to $1.18 per million Btu for western coal, and a range of $1.93 to $3.07 per million Btu for mid-sulfur eastern coal.

Exhibit A-3 also does not have a per-million-Btu price listed for each contract comparable to the list in Mr. Hoffman's testimony at page MGH-7. But a review of Mr. Hoffman's list illustrates the significance a single contract can have on cost. Using the cents-per-million-Btu information, a rough average cost (weighted by tonnage) can be computed for the contracts listed of approximately $1.05 per million Btu. If what appears to be the oldest contract on that list, shown on line 2, is excluded, the rough

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[28] See Tr 67.
[29] See Gallaway, Tr 54 (9.1 million tons from contract and annual supplies; 1.2 million tons from the spot market).

weighted average cost rises to $1.18 per million Btu. The point of this rough calculation is to show that a change in the layers in a portfolio over time can have a significant impact on cost.

MEC also rejects Consumers' observation that Detroit Edison is expecting significant cost increases in 2011. Mr. Gallaway testified: "It is also believed that much of the 32.4% increase that Detroit Edison is reporting in their 2010 PSCR plan between years 2010 and 2011 (calculated from Mr. Sansoucy's Exhibit MEC-9) is due to expiring transportation contracts and the alignment of their new transportation contracts to the current market."[30] MEC notes that Consumers is also expecting its costs to increase 20%, and contends:

> If both utilities are projecting big increases in transportation costs next year, leading to corresponding increases in their projections of system coal costs, it is hard to see how the age or potential expiration of Detroit Edison's transportation contracts explains the big difference in overall cost or provides a compelling reason why the coal costs of the utilities should not be compared.[31]

But there is a significant difference between a 20% increase and a 32.4% increase, so it is not appropriate to conclude that the utilities are projecting corresponding increases. Moreover, a review of the five-year forecast of coal costs in Consumers' plan, although not presented on a per-Btu basis, shows that Consumers is projecting an increase of 27% over the period 2010 to 2014 on a per-ton basis,[32] while Detroit Edison is projecting an increase of over 50% on a per-Btu basis as reflected in Exhibit MEC-9.

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[30] See Tr 72.
[31] See MEC brief at 14.
[32] Compare projected 2010 coal costs per ton in Exhibit A-4 to the 2014 projections in Exhibit A-6.

MEC also rejects “layering” as a basis for differences in cost, contending that Consumers has not established that layering is a reasonable and prudent practice. MEC cites Consumers’ discovery response in MEC-21, quoted in MEC’s brief at page 7, indicating it has not studied or evaluated its average coal cost in comparison to the national average. MEC argues: “The bare statement in Gallaway’s testimony that the layering approach minimizes price and supply risk does not demonstrate that the plan is reasonable and prudent, especially when the projected cost produced by the plan is comparatively as high as it is.”[33] In making this argument, MEC appears to ignore the purpose of the statement, to explain that layering helps protect ratepayers from volatility and to ensure availability of supplies. These are valid goals in planning, and were presented to explain why the company’s coal costs cannot be evaluated simply against current market prices.

2. Fuel Blend Issues

In differentiating Consumers and Detroit Edison, Mr. Gallaway identified plant-specific pollution control requirements, along with differences in plant age and size, as reasons why the blends of coal burned by each utility would be expected to differ. With regard to the pollution control requirements, Mr. Gallaway testified:

> The type of emission limits specified in the [Renewable Operating Permit] (“ROP”)] for SO2 impacts the types of coals that can be burned at each facility. The company owning the facility independently and uniquely determines its strategy for meeting the ROP requirements through a combination of plant modifications, operation, and fuel selection. Consumers Energy has determined it can meet the ROP requirements utilizing the fuel specifications provided in discovery and in Exhibit MEC-7. In 2010, this includes mostly low sulfur western coal from the Powder River Basin and some low sulfur eastern coal and small amounts of mid sulfur eastern coal from Central Appalachia. In Detroit Edison’s 2010

[33] See MEC brief at 8.

> PSCR plan, they have indicated that like Consumers Energy they will be burning low sulfur western coal from the Powder River Basin and eastern coals from Central Appalachia. Unlike Consumers Energy, in Detroit Edison's coal mix will also be lower-cost high-sulfur coal from Northern Appalachia.
>
> The differences in the ROP's between generating facilities and between companies, and the impact the ROP has on the fuels that can be burned at each site discredits Mr. Sansoucy's claim that Consumers Energy's coal cost should be similar to Detroit Edison's because they each "operating in the same state." [34]

MEC disputes the significance of plant-specific air pollution control permitting, contending that air emissions limits should be essentially the same for the utilities' plants. This ignores Mr. Gallaway's testimony, quoted above, that each plant will meet its emissions requirements with a unique mix of fuel blends and other mechanisms, e.g. capital expenditures.[35] A relationship between fuel cost and capital expenditures has long been acknowledged by the Commission.[36] Mr. Sansoucy also recognized this relationship, testifying: "If Consumers must make capital improvements in its generating facilities to enable the company to reduce its coal cost per million BTUs, the recovery of those costs could be addressed in a rate case."[37]

MEC also contends that Consumers has failed to establish that different mixes of coal types burned by Consumers and Detroit Edison plants could account for a cost difference between the utilities. To MEC, the two companies have plans to purchase similar portfolios of coal:

> [Mr. Gallaway] states in his direct testimony that 82.8% of Consumers' total coal burn requirements in 2010 will be met by the lowest-cost

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[34] Tr 70-71.
[35] Also see Gallaway, Tr 106.
[36] See, e.g. Case No. U-6381 (September 27, 1983 order), at page 2, explaining boiler modifications required to burn low-sulfur western coal.
[37] See Tr 284.

> western coal. That means only 17.2% of Consumers total requirement will come from the higher-cost eastern coal. By comparison, Detroit Edison projects that about 18.1% of its total requirement will be met by higher-cost eastern coal.[38]

MEC reasons:

> [T]he difference in cost attributable to Detroit Edison buying some lower cost Northern Appalachian coal comprises no more than a fraction of the [18.1%][39] of Detroit Edison's overall coal requirements that are projected to be met with eastern coal. And whatever fraction of the [18.1%] this difference represents, it is offset at least in part by the almost 1% more of Detroit Edison's requirements that will be met with eastern coal than Consumers' requirements. (The price difference between Eastern and Western coal in the exhibits is much larger than the price difference between Northern and Central Appalachian coal).[40]

While MEC contends that Consumers and Detroit Edison each purchase a similar amount of western coal and thus that any difference in type of eastern coal cannot account for a difference in coal costs between the companies, these broad assertions are not supported by the limited evidence in this record.

First, MEC has not established that both Consumers and Detroit Edison plan to use the same proportions of western and eastern coal. Consumers plans to use approximately 82.8% low-sulfur western coal from the Powder River Basin to meet its coal needs; it plans to meet the remainder with a combination of low-sulfur and mid-sulfur eastern coal. Mr. Gallaway testified that he understands Detroit Edison intends to use at least some lower-cost high-sulfur eastern coal. The testimony from Detroit Edison's 2010 plan case, officially noticed, makes clear that Detroit Edison intends to burn only "over 70%" low-sulfur western coal, and thus as much as 30% eastern coal.[41]

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[38] See MEC brief at 9.
[39] 17.2% in original, but this appears to be an error.
[40] See MEC brief at 10.
[41] See Hoffman testimony, Case No. U-16047, page MGH-9. The 18.1% eastern coal computation made by MEC in its brief at page 9, note 19, is based on Detroit Edison's list of coal contracts, which includes

While the western coal appears to be the least-expensive type of coal purchased, the fact is that the two companies do not appear to purchase similar portfolios of coal by type.

Nor does MEC appear to be correct that cost differences between types of eastern coal are not as significant as cost differences between eastern and western coal. MEC argues in its brief: "The price difference between Eastern and Western coal in the exhibits is much larger than the price difference between Northern and Central Appalachian coal."[42] Mr. Gallaway testified that the high-sulfur eastern coal comes from Northern Appalachia. Mr. Sansoucy presented Exhibit MEC-8, however, which shows that for 2009 and 2010, the difference in cost between Powder River Basin western coal and coal from Northern Appalachia was expected to be on the order of 50 cents per million Btu, while the cost difference between coal from Northern Appalachia and Central Appalachia was expected to be approximately $1.00 per million Btu. Within the category of Central Appalachian coal, the low-sulfur coal will be more expensive than the mid-sulfur coal. Paying an additional dollar per million Btu for 18% of a coal portfolio would add 18 cents to the cost per million Btu—not a trivial potential difference as MEC suggests. But again, because the two utilities do not purchase the same portfolios of coal, it is not possible on this record to draw inferences about the reasonableness or prudence of Consumers' purchases based simply on a comparison of delivered prices.

3. Transportation

only low-sulfur western coal and mid-sulfur eastern coal, but Detroit Edison also plans to meet its coal needs with spot market purchases, reducing the western coal component to as little as 70%.

[42] MEC brief at 10; see also Sansoucy at Tr 294-295.

Mr. Gallaway also testified that transportation costs should not be expected to be the same for Detroit Edison and Consumers because the delivery locations vary. He gave as examples two Consumers plants (JHCampbell and JRWhiting) that are served by only one rail carrier, and indicated that "generally speaking, captive shipments experience higher transportation rates than non-captive shipments . . . due to the lack of competition."[43] Consistent with Mr. Gallaway's testimony, in describing Detroit Edison's transportation costs, Mr. Hoffman testified:

> The ability to blend and burn coals from several coal supply regions along with utilizing multiple transportation options has provided the Company with the leverage to negotiate some of the most competitive delivered fuel prices available.[44]

MEC dismisses this example: "The problem is that the differences between captive and non-captive shipments are too small to explain or distinguish anything."[45] MEC's brief reviews transportation costs shown in Exhibit MEC-22, to assert that:

> The maximum difference in transportation costs between a plant that receives captive shipments and one that does not is \$0.17 for eastern coal (Campbell vs. Cobb) and \$0.07 for western coal (Whiting vs. Karn/Weadock). And the least expensive transportation costs for both types of coal are at plants Gallaway describes as being serviced by only one carrier: Campbell (for western coal) and Whiting (for eastern coal).[46]

A review of Exhibit MEC-22, however, shows that MEC reads more into the exhibit than the information presented there would justify. First, Exhibit MEC-22 shows transportation costs for each of four plants by "eastern" and "western" coal type. It does not provide contract-specific pricing information, so it is not possible to tell whether

[43] See Tr 71.
[44] *Id.*
[45] Brief at 12.
[46] Brief at 13.

"captive" and "non-captive" shipments are covered by a single contract.[47] Mr. Gallaway testified: "Companies with both captive and non-captive shipments are sometimes able to leverage volumes between plants to obtain somewhat lower rates at the captive plants."[48] And while MEC identifies shipping costs that are the lowest shown in Exhibit MEC-22 for Campbell (for western coal) and Whiting (for eastern coal), the corresponding charges for Campbell (for eastern coal) and Whiting (for western coal) are the highest shown. It is not possible to conclude, as MEC's argument suggests, that the maximum difference in transportation costs for non-captive shipments compared to captive shipments is 17 cents for eastern coal and 7 cents for western coal.

Mr. Gallaway testified that the company negotiated all new rail transportation contracts this year, and that transportation costs have increased significantly.[49] MEC disputes that this is relevant, contending that higher transportation costs for Consumers call into question the reasonableness of those costs. Yet no party refuted Consumers' testimony that transportation costs have increased and are expected to continue to increase. As explained above, Detroit Edison is projecting its costs to increase at a greater rate over the next five years than Consumers.

Mr. Gallaway also pointed to Detroit Edison's relationship with a subsidiary, Midwest Energy Resources Company ("MERC") as example of a cost-advantage favoring Detroit Edison. His statement was supported by Mr. Hoffman's testimony in Detroit Edison's 2010 plan case:

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[47] There are five rail transportation contracts, all recently renegotiated, and all competitively bid. See Gallaway, Tr 53, 71-72.
[48] See Tr 71.
[49] See Tr 53.

> The company continues to aggressively market coal and transshipment services to third parties through its subsidiary, Midwest Energy Resources Company (MERC). Third party revenues and the equity received from MERC's joint venture contribute to a significant reduction in Detroit Edison's fuel expense and thus, ultimately, the rates for Detroit Edison electric customers.[50]

4. Conclusion

Because Consumers has explained that a broad comparison of its total as-burned coal costs to those of Detroit Edison does not establish that Consumers' costs are unreasonable, and because the focus in this Act 304 proceeding is the reasonable and prudence of Consumers' power supply decisions, this PFD recommends that MEC's recommended $97 million reduction in power supply costs be rejected. Based on the evidence in the record of this proceeding and the arguments of the parties, this PFD also concludes that the examples of key differences between the utilities identified by Consumers are of sufficient magnitude to explain the difference in coal costs and that Consumers' coal and coal transportation decisions are reasonable and prudent.

B. Zeeland Natural Gas Costs

MEC and the Attorney General also seek a reduction in power supply costs attributable to natural gas purchases for the Zeeland plant.

Consumers projects that the Zeeland plant will use approximately 9.5 million Mcf of natural gas, costing a total of approximately $60 million in 2010, [51] which equates to a delivered cost of $6.37 per Mcf. Mr. Gallaway testified that Consumers uses a third

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[50] See page MGH-10, Case No. U-16047.
[51] See Exhibit A-5.

party to provide natural gas supply to Zeeland.[52] He developed the cost projection on Exhibit A-5, and explained:

> The price of gas for the Zeeland plant is based on the gas market prices (monthly NYMEX) provided by the Risk Management Department [of Consumers Energy] with transportation service provided by SEMCO and ANR.[53]

MEC's witness Mr. Sansoucy obtained through discovery the NYMEX price strip Consumers relied on in making its forecast, Exhibit MEC-11. He testified that the average of the twelve monthly NYMEX prices for 2010 shown in Exhibit MEC-11 is $5.83 per Mcf,[54] and he recommended using this figure in place of the $6.37 per Mcf cost figure the company used to compute power supply costs. This recommendation results in a reduction of approximately $5.1 million in total power supply costs, as shown in MEC-12. He further testified to the reasonableness of this recommendation, indicating that: "[I]t is well known that there is currently a glut of natural gas in the North American system, and so it is highly likely that the cost of natural gas will be lower than even the projected 11-month price."[55]

In rebuttal testimony, Mr. Gallaway responded that the NYMEX prices reflect transportation only to the Henry Hub in Louisiana. The 54-cent difference between Mr. Sansoucy's projection of $5.83 per Mcf and the company's projection of $6.37 per

[52] See Tr 60-61.
[53] See Tr 62.
[54] The prices are stated in MMBtu, but the parties use Mcf and MMBtu interchangeably in their calculations, so this PFD uses Mcf throughout.
[55] See Tr 285. Note that the 11-month price Mr. Sansoucy refers to is the average of 12 monthly Nymex values for each of the months in 2010.

Mcf, Mr. Gallaway testified, is the cost to transport the gas from the Henry Hub to Zeeland.[56]

In surrebuttal, Mr. Sansoucy continued to challenge the company's $6.37 per Mcf cost projection, contending it will overcollect the actual cost of gas. He testified that the projection seemed high to him in light of additional information. His Exhibit MEC-16, containing data reported by the Energy Information Administration of the U.S. Department of Energy, shows that the delivered price of natural gas to Michigan for the electric power sector was $4.52 per Mcf for 2009, and the delivered price of natural gas to Michigan for electric utilities was $5.85 per Mcf. Exhibit MEC-17 shows that Consumers' actual delivered cost of gas for Zeeland in 2009 was $5.39 per Mcf. Mr. Sansoucy testified that there is no reason to believe that natural gas prices will increase significantly this year.[57]

Mr. Sansoucy also challenged the transportation cost estimate of 54 cents per Mcf, indicating it seemed excessive based on information from FERC, presented in Exhibit MEC-15, showing that the average rate paid to ANR for transportation was only 20 cents per Mcf.

In his second rebuttal testimony, Mr. Gallaway testified that the company's natural gas forecast was based on the latest pricing available when the forecast was made.[58] He presented Exhibit A-30 to show actual natural gas prices at the Henry Hub for the period 2003 through March 2010, and the company's 2010 PSCR projections for comparison. Based on Exhibit A-30, Mr. Gallaway testified that current prices showed a

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[56] See Tr 75.
[57] See Tr 293-294
[58] See Tr 81-82.

“close alignment” with the company’s forecast, and did not suggest the company’s forecast was out of line.

Regarding transportation costs, he testified that the 20-cent average cost figure cited by Mr. Sansoucy for transportation on ANR is not appropriate to use because as a system-wide average, it does not reflect the distance to the appropriate delivery point, or the additional cost of firm transportation over interruptible transportation.[59] He presented Exhibit A-29 to show that interruptible transportation on ANR to the appropriate receipt point could be up to 33 cents per Mcf, with firm transportation costing more. And he explained that transportation on an additional pipeline (SEMCO) is required to bring the gas all the way to Zeeland, at an additional cost.[60]

On cross-examination, Mr. Gallaway and Mr. Polena were both asked about current NYMEX price projections, and acknowledged recent prices had been lower than the company’s forecast.

Mr. Gallaway was also asked about the third-party contract Consumers has to supply Zeeland. He testified that the company’s third-party contract was with BP Canada for the first part of 2010, and then with EDF Trading for the later part of 2010.[61] He testified that the third-party contract includes transportation, so that the company does not pay ANR or SEMCO directly. Although on cross-examination Mr. Gallaway thought the third-party contract had separate provisions for supply and transportation, on redirect, he testified that the contract was an “all-in” price.

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[59] See Tr 78-79.
[60] He later testified that the SEMCO pipeline charge is 24 cents per Mcf. See Tr 88.
[61] Consumers Energy refers consistently to its third-party contract in the singular, so this PFD does likewise, although it is unclear on this record whether the company has separate or materially different contracts with BP Canada and EDF Trading.

In its brief, MEC argues for a reduction of $17.5 million in the estimated power supply costs for the Zeeland plant, contending the company's forecast of natural gas prices is excessive. MEC also argues that Consumers did not support its transportation cost estimate. The Attorney General supports MEC's proposed adjustment, and also takes issue with the utility's transportation cost estimate. Consumers responds that its natural gas supply contract for Zeeland was competitively bid, that its natural gas price estimates were reasonable when they were made, and finally, that the company monitors its PSCR factor continually and will reduce the factor if its estimate proves to be overstated.

The dispute over transportation costs is integrally linked to Consumers' third-party contract, which is discussed in subsection 1 below. The dispute over the appropriate natural gas price projection to use in the factor calculation is addressed in subsection 2.

1. Third-Party Contract

Both MEC and the Attorney General contend that Consumers has failed to support its transportation cost estimate of 54 cents per Mcf. Staff objects to any reliance on system-wide averages to determine transportation costs, and asks the Commission to use Consumers' actual costs. At the heart of the matter, however, there is no evidence on this record exactly what those transportation costs are.

While Mr. Gallaway was responsible for projecting the company's natural gas costs, it appeared that he was not familiar with the third-party contract. He testified that the contract provides benefits to the company in terms of flexibility of operations:

> Consumers Energy utilizes a third party to provide gas supply to the Zeeland plant. Spot gas pricing is provided by the third party on a daily basis to bid Zeeland into the MISO market and actual purchases are made by the third party in the day ahead, intra day and real time gas markets to balance purchases against the actual burn. Pricing is based on several gas indices tied to several step changes in gas volume, which has the combined effect of assuring gas delivery in the summer when the plant is most likely to run and also to keep the price of gas lower when high volumes are required. A gas delivery tolerance provided for in the third party contract provides for a certain amount of storage that enables us to mitigate some of the risk of purchasing too much gas ahead of time when the plant burns less than expected. Additional interruptible storage is also available most of the year on the ANR pipeline system.[62]

He also testified that the contract was competitively bid and that the company selected "the lowest-cost provider that we believe would provide the gas requirements on a firm basis that we felt were necessary to operate the Zeeland plant."[63]

But Mr. Gallaway could not explain why the ANR prices were reasonable to use to model the third-party contract costs as shown in this colloquy from cross-examination by counsel for the Attorney General:

> Mr. Gallaway: Just to clarify . . . as I mentioned before, we have a third party which manages this for us, and they would have a number of . . . instruments or contracts on ANR that enables them to move the gas . . . on a firm basis.
>
> So I can't explicitly identify how this specific ANR tariff ties directly to what we pay because it's a . . . third-party arrangement.
>
> Mr. Erickson: Well, is the price dependent on the price they pay to ANR?
>
> Mr. Gallaway: Yes, I would anticipate so.
>
> Mr. Erickson: Well, if it isn't, then, of course, Exhibit A-29 has nothing to do with the price of gas that you buy from BP or the other supplier; am I right?

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[62] Tr 60-61.
[63] See Gallaway, Tr 129.

Mr. Gallaway: I'm not sure I understood.

Mr. Erickson: Well, if you pay a price to BP for delivery at Zeeland, and you're getting both the commodity and the transportation FOB Zeeland, and that price is fixed by contract, then the price they pay would be irrelevant to the price that you're projecting for the cost of gas burned at Zeeland; am I right?

Mr. Gallaway: When you say the price that –

Mr. Erickson: BP or the other supplier would pay would be irrelevant. And if BP is paying the transportation to ANR and the – and your contract doesn't call for you to reimburse them directly on the basis of what they pay to ANR, then A-29 doesn't have anything to do with the price you project for gas.

Mr. Gallaway: That would be correct.

Mr. Erickson: So as I understand it, BP's contract with you for the delivery of gas to Zeeland incorporate or is – that price is adjusted as the price – the transportation prices of ANR are adjusted; am I correct?

Mr. Gallaway: We have a contract rate with BP, and that what we would pay them.

Mr. Erickson: Okay. And is that contract rate a delivered all-in price, or is it a contract rate that has a commodity component and a transportation component?

Mr. Gallaway: A commodity and transportation.

Mr. Erickson: Okay. And does the transportation component of that contract track prices ANR would charge?

Mr. Gallaway: I don't know.[64]

In a continuation of this colloquy, Mr. Gallaway was expressly asked to state the pricing terms, and he responded:

> The only information that I have with me doesn't explicitly state the details of how we get the relationship to the Henry Hub or the NYMEX Henry Hub value adjusted with transportation. All that I have with me basically

[64] See Tr 120-131.

> supports that – the value that we anticipate paying the third party is the NYMEX value plus approximately 30 cents.[65]

After this, on redirect, Mr. Gallaway testified that the contract was a single price, or "all-in", agreement. Further, he acknowledged that his Exhibit A-29 was irrelevant, not related in any way to the costs paid by Consumers to the third party.[66] Following this testimony, Mr. Gallaway did not reconcile this new information to his initial testimony that the price of gas for Zeeland is based on NYMEX prices with transportation service provided by ANR and SEMCO, or his rebuttal testimony that the difference between the NYMEX average of $5.83 and his price projection of $6.37 represents the cost to transport the gas from Henry Hub to Zeeland. Thus, there is no basis on this record to conclude that Consumers has accurately modeled the costs it will pay for natural gas for the Zeeland plant under the third-party contract.

Because Consumers has not established the basis for the charges under the contract, and because the key company witness was not able to explain the contract and at times misunderstood or was not informed about key provisions of the agreement, this PFD recommends that the Commission find that the company has not established that its third-party contract to supply Zeeland is reasonable and prudent. Consumers should be prepared to support the reasonableness and prudence of this agreement in the reconciliation.

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[65]While Mr. Gallaway uses the figure of 30 cents here, his rebuttal testimony indicates transportation costs are assumed to be 54 cents: the difference is presumably the 24 cents charged by SEMCO, although it is not clear on this record.

[66] See Tr 135.

2. Zeeland Plant Power Supply Costs

As explained above, Consumers' cost projection for Zeeland is based on a commodity cost projection of $5.83 per Mcf, plus an additional 54 cents per Mcf for transportation. The commodity cost component is based on the July 28, 2009 NYMEX strip. MEC contends that natural gas prices have fallen since that forecast was prepared, and urges the Commission to reduce the power supply cost projection by $17.5 million.

To calculate this $17.5 million adjustment, MEC uses the value of $4.52 per Mcf taken from Exhibit MEC-16, multiplied by the company's forecast Zeeland volumes of approximately 9.5 million Mcf, to determine total Zeeland natural gas costs. MEC also asks the Commission to take official notice of more recent NYMEX data for 2010. Using the value of $4.44 per Mcf that MEC attributes to an April 20, 2010 NYMEX strip, MEC computes an alternative cost reduction of $18.3 million.[67]

Consumers' reply brief does not directly address MEC's proposed reduction, or its request that the Commission take official notice of recent NYMEX data. Instead, the company argues that it manages its factor and will lower it as costs fall below projected values.[68]

MEC does not find Consumers' assurances that it will manage its factor satisfactory, and cites prior Commission decisions indicating that the most recent data should be used in factor calculations.[69] As MEC correctly argues, while the Commission has cautioned the parties against spending excess time debating spot

[67] See MEC brief at 24-25 and n60.
[68] See Consumers Energy reply brief at 11-12.
[69] See MEC brief at 25 n63.

market price forecasts, the Commission has also expressed a preference for using current data.

MEC is also correct that more current information indicates the company's 2010 price forecast is too high. The July 28, 2009 NYMEX price strip Consumers used to forecast an average natural gas commodity cost of $5.83 per Mcf showed monthly prices ranging from $5.295 to $6.727 per Mcf. Consumers' Exhibit A-30 shows that gas costs for the first 3 months of 2010 were well below the company's initial forecast for those months, and averaged $5.30 per Mcf. Mr. Gallaway was not aware of more recent price projections when he testified in April.[70] Mr. Polena indicated that he looks at natural gas futures prices on a daily basis, but he doesn't determine an annual average price from the strip prices he reviews. The last time he checked, prices were around $4.00 per Mcf for some of the summer months, with prices for the end of the year around $5.00 or higher. While he believed the highest prices he had seen this year had been around $6.00, recently the highest prices he had seen had been around $5.50.[71] Note that Mr. Polena's Exhibit A-15 shows that July and August are the months in which the company has the highest natural gas use. Exhibit A-30 and the testimony of these witnesses buttress Mr. Sansoucy's testimony that he does not expect prices to increase significantly in 2010 over 2009 levels, and his related claim that his original estimate of $5.83 per Mcf is more reasonable as a delivered price than the company's projected cost of $6.37 per Mcf.

MEC's $17.5 million adjustment, however, is much larger than the one supported by Mr. Sansoucy's testimony. The $4.52 per Mcf used as the delivered gas cost in

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[70] See Tr 91-93.
[71] See Tr 232-4.

MEC's recommended adjustment comes from Exhibit MEC-16. Although this document was prepared in March, 2010, the data reported are for 2009 and 2008, and the $4.52 figure itself is described as "the average cost of natural gas delivered for electricity generation" for the "electric power sector" for 2009. Exhibit MEC-16 also shows the average delivered cost of natural gas for "electric utilities" in 2009, a higher figure of $5.85 per Mcf.

MEC also calculates an alternative cost reduction of $18.2 million, based on a NYMEX price projection of $4.44 MEC asks the Commission to take official notice of. But this estimate makes no provision for transportation costs from the Henry Hub, and thus would understate the company's expected costs. Nor is it consistent with MEC's criticism of Consumers for relying on a single day's NYMEX strip for its commodity cost projection.[72]

Because the $17.5 million adjustment is based only on 2009 costs for the entire electric power sector, and because the $18.2 million adjustment makes no provision for provision for transportation costs from the Henry Hub and relies on a single day's NYMEX strip, this PFD recommends rejection of both these adjustments as unsupported on this record. Instead, this PFD recommends using Mr. Sansoucy's original estimate of $5.83 per Mcf, which his surrebuttal testimony establishes is a reasonable projection given more recent information. This results in an adjustment of $5.1 million as shown in his Exhibit MEC-12. Subtracting $5.1 million from the total power supply costs shown on line 8 of Exhibit A-1 results in a PSCR factor of negative $0.00066 per kWh.

[72] See MEC brief at 19; Sansoucy at Tr 284-285.

Using the company's estimate of 54 cents for transportation costs, this projection is consistent with annual NYMEX price of $5.29 per Mcf, relatively close to the $5.30 average for the first three months, recognizing projections for subsequent months have been as low as $4.00.[73] It is also significantly above Consumers' 2009 delivered cost of natural gas to Zeeland of $5.39 per Mcf, as reflected in Exhibit MEC-17, page 6.

In making this recommendation, this PFD does not recommend any specific adjustment to the company's transportation cost projection. Although as explained in subsection 1 above, the company has failed to establish that its cost model correctly predicts the third-party contract costs, or to establish that the third-party contract is reasonable and prudent, the company obviously must incur some cost to transport the gas from the Henry Hub to Zeeland. While 54 cents may not be an accurate value, there is no other value supported on this record for use as an alternative. While Mr. Gallaway's understanding of the third-party agreement was limited, his testimony is convincing that Consumers would pay more than the ANR system-wide average transportation cost of 20 cents per Mcf in the absence of the third-party agreement, and no party challenged his testimony regarding the 24-cent-per-Mcf SEMCO charge.

C. Load Projections/Sales Forecasts

MEC contends that the forecast generation requirement underlying the company's 2010 plan is unreasonable, and was unreasonable when it was filed in September of 2009. MEC cites Mr. Warriner's projected 0.2% annual growth in PSCR sales for the forecast period, and the historical decline in sales of -0.2% over the time

[73] See Polena, Tr 232.

period 2000 to 2008 identified by Mr. Warriner.[74] It then argues that the 39,387,149 MWh total system generation projected for 2010 in Mr. Warriner's Exhibit A-24, page 1 is 4.4% higher than the company's actual generation in 2009 of 37,727,226 MWh as reported in the company's FERC Form 1, page 7 of Exhibit MEC-19, lines 20 and 28. MEC emphasizes that it believes the forecast for 2010 was unreasonable when it was filed:

> [T]here is no basis in the record of this case from which to conclude that the 2010 forecast was a reasonable one for the plan when it was submitted. Total generation in 2009 was 1,659,923 MWh lower than Mr. Warriner's forecast for 2010. Mr. Warriner prepared the forecast in September of 2009. There is no evidence that indicates there was a dramatic reduction in the Company's generation during the last three or four months of 2009 compared to the first eight or nine months of that year. Therefore, there is no basis from which to conclude that the Company was not on track for something in the neighborhood of 37 million MWh of total generation in 2009. Therefore, there is no basis from which to conclude that the Company's September 2009 forecast of an almost 1.7 million MWh increase in 2010 generation requirements over 2009 was reasonable at the time it was submitted.[75]

The Attorney General supports MEC's claim, asserting without explanation that the negative PSCR factor requested by Consumers, i.e. a total factor below the recently-established base, shows that the company's forecast is overstated: "CECo's admitted need to reduce the allowance in base rates for PSCR expenses by charging a negative PSCR also supports MEC's argument that CECo's forecast in this case is too high."[76]

As indicated above, Consumers' response to MEC's argument is only that MEC did not present its analysis through a witness. Staff objects to what it characterizes as

[74] See Tr 248.
[75] See MEC brief at 27-28.
[76] See Attorney General reply brief at 7.

MEC's "surface level" comparisons, but does not address MEC's arguments in greater detail. Since the Attorney General's argument was presented in a reply brief, the parties were not able to respond. Based on the record, however, this PFD recommends that the Commission reject MEC's and the Attorney General's objections to the forecast.

First, MEC appears to be drawing an erroneous comparison between the FERC report in Exhibit MEC-19 and Mr. Warriner's Exhibit A-24. Mr. Warriner's 2010 projection of "total system generation requirements" for 2010 is 35,634,977 Mwh, as presented in Exhibit A-24, page 3 and shown on line 9 of Exhibit A-1. Page 1 of his Exhibit A-24 includes both PSCR generation and a hypothetical Retail Open Access generation, as shown from the following pages 2 and 3, where ROA generation is subtracted from the page 1 totals to determine what is labeled "monthly generation requirements to be supplied by Consumers Energy". Since the company does not generate energy to serve the ROA load, the numbers on page one of Exhibit A-24 show only a step in Mr. Warriner's analysis of translating forecast electric deliveries into generation requirements, rather than having the meaning ascribed to them by MEC.

Second, MEC's argument that 2009 sales are a better predictor of 2010 sales than Mr. Warriner's model is without evidentiary support on this record. Even assuming MEC has properly characterized Exhibit A-24, page 1, and thus that Consumers' plan implicitly projects an increase of 4.4% in total generation, that difference in and of itself does not make Consumers' 2010 forecast unreasonable. Consumers' initial brief explains the detailed modeling performed by Mr. Warriner, quoting his testimony as follows:

> The forecast reflects a separate projection for each customer class and, where appropriate, analyzes certain classes in more detail. Projection techniques vary from category to category based upon the availability of information, the accuracy required in the forecast, and the need to determine the influence of specific input assumptions for each category. Forecast methodology was the combined result of regression (statistical) models, customer input, and professional judgment. The forecast was based primarily on regression analysis. Independent variables in the regression analysis include economic variables that are obtained from a separate economic forecast, weather variables, and trend variables. In addition, the impacts of future factors, or 'forward-looking' items (such as expected customer use changes due to the Company's Energy Optimization Plan, and the expected introduction of Plug-In Hybrid Electric Vehicles) not fully present in past data, are applied as adjustments to the forecast when appropriate.[77]

While it may perhaps be that last year's sales are a better predictor of this year's sales than the multivariate modeling used by Consumers, there is no evidence to support that claim on this record.

MEC cites the Commission's decision in Case No. U-15675, Consumers' 2009 plan case. MEC's argument in this case is not the same as the argument presented in Case No. U-15675, when the company's own forecast changed after its initial filing. Here, instead, MEC and the Attorney General rely only on a difference between 2009 actual results and 2010 forecast sales to establish that the forecast must be unreasonable, without establishing that 2009 sales are a better predictor of 2010 sales (or generation requirements) than the company model.

And finally, that the PSCR factor is negative due to the base factor established in the last proceeding simply does not establish that the company's sales forecast is overstated. Note that negative factors have been established in prior PSCR cases, with

[77] See Tr 243-244.

no adverse inference drawn.[78] Total costs rise and fall for a variety of reasons. The Attorney General has failed to establish a logical link between the reasonableness of the forecast and the size of the PSCR factor relative to the base.

D. Merchant Plant Issues

MCL 460.6a(7) and (8), added by 2008 PA 286, provide for additional payments, above contract requirements, to certain merchant plants generating electricity from wood or solid wood wastes, referred to as “biomass merchant plants” or “BMPs”. The additional payments are for recovery of “reasonably and prudently incurred actual fuel and variable operations and maintenance expenses.” MCL 460.6a(9) directs the Commission to issue orders permitting the biomass merchant plants to recover the additional allowed amounts, and permitting the utilities to recover the additional allowed amounts from ratepayers. In its August 11, 2009 order in Case No. U-16048, the Commission approved procedures for implementing these provisions, which include the following:

> A. In its power supply cost recovery (PSCR) plan filings, CECo will estimate the total payments to be made to the BMPs and include that amount in its PSCR plan and factor.
>
> B. CECO’s actual payments to the BMPs, as well as any additional amounts due to the BMPs, will be reviewed and approved, amended or disapproved by the MPSC in the context of CECo’s annual PSCR reconciliation proceedings and will provide the support necessary for CECo’s full recovery of all reasonable and prudent payments to the BMPs pursuant to subsections (7), (8) and (9) of MCL 460.6a.

Consistent with these procedures, Mr. Polena testified that he had included payments to the biomass merchant plants on line 48 of his Exhibit A-14, which shows a

[78] See, e.g. Case No. U-10710 (December 20, 1995 Order), at n1.

monthly amount of $1 million for an annual total of $12 million.[79] He further explained that the $12 million represents Consumers' maximum liability,[80] and that the company did not have the information available to them at the time he prepared the estimate that would make it possible to determine how much the biomass merchant plants would ultimately recover. He agreed that, pursuant to the Commission's order and statute, reasonableness and prudence and recoverability of actual biomass merchant plant billings would be determined in the reconciliation.

In his initial brief, the Attorney General requested that the Commission order in this case expressly defer a final decision on merchant plan recovery under MCL 460.6a(7), (8) and (9) to the reconciliation. In his reply brief, the Attorney General clarified his position. The Attorney General is concerned to ensure that reasonableness and prudence of supplemental merchant plant payments under the relevant provisions is preserved for reconciliation. Focusing on the language in MCL 460.6j(12), the Attorney General asserts that to review the payments in the reconciliation phase, the Commission will be required to make a determination that the costs could not have been adequately reviewed in the plan proceeding. MCL 460.6j(12), in pertinent part, directs the Commission in a reconciliation as follows: "The Commission shall consider any issue regarding the reasonableness and prudence of expenses for which customers were charged if the issue was not considered adequately at a previously conducted power supply and cost review."

The Attorney General explains:

[79] See Tr 215, 225-227.
[80] MCL 460.6a(8) caps liability for each utility at $1,000,000 per month.

> The point of the Attorney General's deferral request is that the evidentiary record in this case is not adequate to allow the Commission to make a final decision regarding reasonableness and prudence. In the alternative, the ALJ should recommend a final order in this case that concludes the order in U-16048 precludes review in this case, and therefore, the parties in this case do not have an adequate opportunity to review reasonableness and prudence.

Consumers' reply brief asserts that the Commission is required to include the estimated payments in the PSCR factor "as a predicate to the analysis of the reasonableness and prudence of these expenses to be conducted in the Company's PSCR reconciliation proceeding." Staff asserts that it is unnecessary to address the issue in this case, since the Commission's order and the procedures specified in that order are clear, and the costs will be reviewed and approved, amended or disapproved in the reconciliation.

Based on a review of the positions of the parties, there is no tangible dispute. The Commission has already provided for the costs to be reviewed in the reconciliation, and the company has acknowledged that the costs will be reviewed in the reconciliation. Pursuant to the established procedures in Case No. U-16048, Consumers did "estimate the total payments to be made to the [biomass merchant plants] and include that amount in its PSCR plan and factor." As Consumers points out, no one is challenging its $12 million estimate by suggesting it is wildly out of range: instead, the company's estimate is based on the statutory maximum under MCL 460.6a(8).

It is difficult to determine what additional assurances, formalities or otherwise, the Attorney General is seeking. Nonetheless, in an effort to avoid further confusion, this PFD concludes that the parties to this case were not able to review the reasonableness and prudence of Consumers' actual payments to the biomass merchant plants, or to determine any additional amounts due them in this plan case proceeding, and that the Commission has clearly preserved this review for the reconciliation proceeding. Since no party challenges the company's $12 million for inclusion in the factor calculation in this proceeding, this PFD concludes the PSCR factor calculation should include Consumers' estimate of the total payments to be made to the biomass merchant plants.

E. Contract Approval

As noted above, Consumers sought approval of two agreements, Exhibit A-19, a power purchase agreement intended to supply the company's Green Generation program, and Exhibit A-20, a revised dispatch agreement. No party opposed the company's request. This PFD recommends that the Commission grant the requested approvals.

IV.

CONCLUSION

For the reasons set forth above, this PFD recommends that the Commission approve the company's 2010 PSCR plan, with the exception of the company's third-party contract to supply natural gas to Zeeland, which should be reviewed in the reconciliation. Further, this PFD recommend that the company's power supply costs be reduced by $5.1 million as shown in Exhibit MEC-12, resulting in a revised maximum power supply cost factor of negative $0.00066 per kWh, also stated as ($0.00066) per

KWh. To avoid any possible confusion in the reconciliation, this PFD recommends that the Commission find that based on its order in Case No. U-16048, the parties were unable to review the reasonableness and prudence of payments to the biomass merchant plants under MCL 460.6a(7) and (8), and thus, in accordance with the Commission's order, those costs will be reviewed in the reconciliation. Finally, this PFD recommends approval of two agreements, Exhibits A-19 and A-20.

STATE OFFICE OF ADMINISTRATIVE
HEARINGS AND RULES
For the Michigan Public Service Commission

Sharon L. Feldman

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Sharon L. Feldman
Administrative Law Judge

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